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NO. _____

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1983

HAROLD V. SIMPSON & COMPANY, Petitioner

VS.

RONALD WILLIAM SHULER, Respondent

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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April 5, 1984

59pp

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The Petitioner HAROLD V. SIMPSON & COMPANY respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit entered in the proceeding on January 20, 1984.

QUESTION PRESENTED

Whether, under 28 U.S.C. §1738, state law governs the collateral effect of a state default judgment in a bankruptcy dischargeability proceeding.

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18 C. WRIGHT, A. MILLER & E. COOPER, Federal Practice & Procedure §4470 (1981) 16,19,20

OPINION BELOW

The opinion of the Court of Appeals is reported at 722 F.2d 1253; that opinion appears in the Appendix. The District Court for the Western District of Texas did not render an opinion. Its order affirming the Bankruptcy Court's decision appears in the Appendix. The memorandum opinion and order of the United States Bankruptcy Court for the Western District of Texas, Austin Division appears in the Appendix.

JURISDICTION

The judgment of the Court of Appeals for the Fifth Circuit was entered on January 20, 1984. A timely petition for rehearing was denied on February 13, 1984. This petition for certiorari is filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

United States Code, Title 28:

> §1738. State and Territorial statutes and judicial proceedings; full faith and credit
>
> The Acts of the legislature of any State, Territory, or Possession of the United States, or copies thereof, shall be authenticated by affixing the seal of such State, Territory or Possession thereto.
>
> The records and judicial proceedings of any court of any such State, Territory or Possession, or copies thereof, shall be proved or admitted in other courts within the United States and its Territories and Possessions by the attestation of the clerk and seal of the court annexed, if a seal exists, together with a certificate of a judge of the court that the said attestation is in proper form.
>
> Such Acts, records and judicial proceedings or copies thereof, so authenticated, shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the courts of such State, Territory or Possession from which they are taken.

United States Code, Title 11:

§523. Exceptions to discharge

(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt -

* * * *

(2) for obtaining money, property, services, or an extension, renewal, or refinance of credit, by -

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition; or

* * * *

STATEMENT OF THE CASE

Harold V. Simpson & Company filed suit in a Texas court against Ronald W. Shuler; Simpson & Company sought to collect a debt. A default judgment which found that the debt was incurred through false pretenses was entered for Simpson & Company. Later, Shuler filed a petition for relief in Bankruptcy Court. Simpson & Company asked that court to determine the non-dischargeability of

the debt. The Bankruptcy Court declared that it was not bound by the findings of the state court. It discharged the debt. Simpson & Company appealed to the District Court, which had jurisdiction under PUB. L. 95-598, Title IV, §405, Nov. 6, 1978, 92 Stat. 2686,(c)(1)(C) (note preceding 28 U.S.C. §1471, governing appeals from the Bankruptcy Court during the transition period.) The District Court affirmed the judgment of the Bankruptcy Court. The Court of Appeals upheld the District Court.

Simpson & Company provided income tax services to Shuler. Shuler did not pay. Simpson & Company sued in a Travis County, Texas Court of Law, claiming that the debt was for obtaining items by false pretenses, both inclusive and exclusive of representations of financial condition. The court found that Shuler,

though duly cited, had not appeared and further found that "Plaintiff's cause of action is based upon a liquidated demand and debt for obtaining by false pretenses the items furnished by Plaintiff, and that Plaintiff is entitled to judgment as prayed for." Shuler did not appeal the default judgment. Months after the judgment, Shuler filed a petition for relief in United States Bankruptcy Court. Simpson & Company filed a Complaint to Determine the Non-dischargeability of the Debt and for Judgment. Simpson & Company stated that the debt "is one for obtaining money, property or services by false pretenses other than a statement respecting financial condition." At trial in the Bankruptcy Court, Simpson & Company relied upon authenticated copies of its original petition and the judgement of the state

court. It contended that the fact issue of whether the debt was incurred by false pretenses had been finally determined between the parties. The Bankruptcy Court, upon trial, stated that it was not bound by those fact findings and that it would not consider them as evidence; the court found for the debtor Shuler. The United States District Court affirmed the decision of the bankruptcy court. Simpson & Company appealed to the Court of Appeals for the Fifth Circuit. It presented two arguments. First, the Bankruptcy Court was bound by statutory full faith and credit (28 U.S.C. §1738) to accept the findings contained in the state court judgment. Second, collateral estoppel bound the Bankruptcy Court to accept the fact issues determined by the state judgment. The Court of Appeals rejected both argu-

ments. It held that the Bankruptcy Court could not discern from the state court record the subsidiary facts upon which this false-pretense allegation was made. Therefore, it said the Bankruptcy Court "....properly refused to accord collateral estoppel effect to the conclusory false-pretense 'determination' in the state court judgment." 722 F.2d at 1258. The Court of Appeals then dismissed the full faith and credit argument. It stated that because in bankruptcy the res judicata or collateral estoppel effect of state court judgments has been limited by competing federal interests, the full faith and credit accorded those judgments may be correspondingly limited. Finding no error in application of collateral estoppel, the Court of Appeals held §1738 was not violated. 722 F.2d at 1258, no. 10.

REASONS FOR GRANTING THE WRIT

1. THE DECISION BELOW CONFLICTS IN PRINCIPLE WITH THE DECISIONS OF THE SUPREME COURT AS TO THE PROPER APPLICATION OF 28 U.S.C. §1738.

Statutory full faith and credit requires a federal court to apply state law in determining the collateral estoppel effect of prior state court adjudication. Allen v. McCurry, 449 U.S. 90,96 (1980). In the decision below the Fifth Circuit mistakenly applied federal collateral estoppel law to determine the preclusive effects of a state court judgment. In an unusual twist, it then used the federal estoppel principles to narrow the scope of statutory full faith and credit. Finally, it failed to examine this curiously limited full faith and credit and it failed to examine the state laws of preclusion which would apply to any adjudication within the

bounds of the newly-narrowed statute. 722 F.2d 1253, 1257-58.

The Fifth Circuit began its error by misreading Brown v. Felsen, 442 U.S. 127 (1979). In that case, this Court found that Congress gave the bankruptcy courts exclusive jurisdiction to decide dischargeability of claims against the bankrupt. That grant of exclusive jurisdiction precluded use of a prior state court judgment as a res judicata bar to an independent dischargeability determination. The Court noted however, if a state court adjudicating a state-law question determined factual issues using standards identical to those of the dischargeability provision, then collateral estoppel would bar relitigation of those issues in the bankruptcy court. The Fifth Circuit cited this statement, but incorrectly extended it.

The Court of Appeals implicitly reasoned that federal law sanctions collateral estoppel in some situations, therefore, federal collateral estoppel principles govern prior findings in those situations. The court explicitly adopted a three-part collateral estoppel test; that test was a statement of federal collateral estoppel principles.

The Fifth Circuit stated that the full faith and credit required under §1738 is manifested by the preclusive effect accorded that judgment. 722 F.2d at 1258, n. 10. It found that the lower courts properly assessed the collateral estoppel effect of the state court judgment. Full faith and credit, it said therefore, was not violated.

The Fifth Circuit's analysis is backward. It should have begun by examining the grant of exclusive jurisdiction and

the full faith and credit statute. If the court found that exclusive jurisdiction could limit the scope of issues which could be decided by the state courts, then it should have applied full faith and credit principles to those issues decided below which did not fall under exclusive federal jursidiction. Those full faith and credit principles are of course a matter of state law. The Fifth Circuit, however, adopted federal principles of preclusion: it relied on the Fifth Circuit's general test for collateral estoppel. 722 F.2d at 1256 n. 2.

If the Fifth Circuit analyzed exclusive jurisdiction and full faith and credit, it would have found that state courts are free to decide subsidiary fact issues. Although a state court decision of dischargeability would con-

flict with the bankruptcy court's grant of jurisdiction, decisions of fact matters and other state legal questions would not. Application of Texas law to the facts found in the Texas judgment might surprise the Fifth Circuit. Under Texas law, a defendant's default operates as a binding judicial admission of the facts alleged by the plaintiff. Rules 241,243, TEX. R. CIV. PROC. A default judgment has the same force and effect as a judgment rendered after a trail on the merits. Thus, the Fifth Circuit not only erred in applying §1738 and federal principles of collateral estoppel, it also reached the wrong result.

The Fifth Circuit's application of general federal - not state - rules of collateral estoppel conflicts in principle with this Court's interpretation of

28 U.S.C. §1738. This conflict and mistaken application justifies the grant of certiorari to review the judgment below.

2. THE DECISION BELOW RAISES SIGNIFICANT AND RECURRING PROBLEMS OF COLLATERAL ESTOPPEL UNDER 28 U.S.C. §1738 IN BANKRUPTCY DISCHARGEABILITY.

The Fifth Circuit's opinion below typifies collateral estoppel discussions in the context of dischargeability. The courts of appeal focus on the grant of exclusive jurisdiction. They provide a variety of approaches to estoppel questions. common to their analyses is a failure to evaluate the role of §1738. Indeed, the Fifth Circuit below is unique: it provides the only appellate decision that cites the statute. The collateral estoppel questions require clarification. They call for a consistent analytical approach to determining the role of the federal courts.

Spilman v. Harley, 656 F.2d 224 (6th Cir. 1981) is a sterling example of the failure to consider 28 U.S.C §1738. The court discussed Brown v. Felsen, supra, and numerous pre- and post-Brown cases concerning collateral estoppel in dischargeability. The Spilman court did not explicitly address the source of estoppel law. It clearly, however, drew estoppel requirements from federal law. Blonder-Tongue Labs, Inc. v. University of Illinois Foundation, 402 U.S. 313 (1971) and Parklane Hosiery Co., Inc. v. Shore, 439 U.S. 322 (1979) provided those requirements. Those cases applied federal rules of preclusion because the court faced prior federal judgments. The Spilman court missed the crucial distinction that state rules of preclusion govern prior state judgments.

Other cases parallel Spilman in their complete failure to mention §1738. In Carey Lumber Co. v. Bell, 615 F.2d 370 (5th Cir. 1980) the court did not mention state estoppel law. Utilizing federal estoppel principles it appeared to condone additional investigation of facts previously determined in state courts. In re Rahm, 641 F.2d 755 (9th Cir. 1981), cert. denied, Gregg v. Rahm, 454 U.S. 860 (1981) did not mention full faith and credit. Nor did In re Comer, 723 F.2d 737 (9th Cir. 1984). Some courts believe that state law of collateral estoppel defines the effects of state findings in subsequent dischargeability proceedings. Davidson v. Lonoke Production Credit Ass'n, 695 F.2d 1115 (8th Cir. 1982); State of Texas v. Wellington Resources, 706 F.2d 533 (5th Cir. 1983). Yet these courts also fail

to mention statutory full faith and credit.

Professors Wright, Miller and Cooper discuss this failure and propose an analytical framework to resolve it. 18 C. WRIGHT, A. MILLER & E. COOPER, Federal Practice and Procedure §4470 (1981) [hereinafter cited as Wright]. The failure even to mention §1738 is common because the courts face a difficult problem. If a state court has entered a valid judgment in the exercise of proper jurisdiction, is a federal court in a subsequent action within exclusive federal jurisdiction bound to honor the same preclusion rules that would apply in the state? The bankruptcy cases cited above, along with numerous lower court bankruptcy cases, avoid the question. Like courts in other areas of ex-

clusive federal jurisdiction, they do not mention full faith and credit.

Wright suggests an analytical framework preferable to such furtive avoidance. An analysis should weigh the specific purposes that underlie the grant of exclusive jurisdiction and balance them against the reasons that justified an exercise of state court jurisdiction.

This Court should apply this analysis to the dischargeability context. The reasons for exclusive jurisdiction in dischargeability are unusually clear. In Brown v. Felsen, supra, this Court noted those reasons. The primary reason is to eliminate the abuse of post-bankruptcy state court collection writs as a means of resolving certain dischargeability questions. The secondary reason is to take dischargeability claims away

from state courts that seldom dealt with federal bankruptcy laws and to give those claims to the bankruptcy court so that it could develop expertise in handling them. Neither reason is of great force here.

There is no danger of abuse in a pre-bankruptcy suit. In addition, the fact question of whether the debt was obtained by false pretenses is one of state law. It is not a seldom-heard question calling for federal expertise.

Other concerns raised in Brown v. Felsen do not apply here. In Brown, this Court feared that application of res judicata would force unnecessary litigation into the state courts. The issue preclusion effect of collateral estoppel does not create that danger. Unlike the question of dischargeability, the fact questions decided below were

directly in issue. Both parties had full incentive to litigate them.

This Court must weigh the reasons that justified an exercise of state court jurisdictions against these weak arguments for an exclusive jurisdiction bar to prior state findings. The question of how the debt was obtained was one of fact. It was properly raised in the state action. As Wright notes, it is difficult to characterize such questions as peculiarly federal.

Issue preclusion applies even if the findings apply state law to historic fact. When state and federal courts independently apply identical standards to the same facts, state law precludes relitigation of such issues. See Becher v. Contoure Labs, Inc., 279 U.S. 388 (1929) in which a state court contract suit decided that an employee-inventor

had wrongfully applied for a patent. He was required to assign the patent to his employer. That judgment precluded his patent infringement suit against another party. Becher has been applied in other areas of exclusive federal jurisdiction.

Securities cases also illustrate preclusion. In three cases, state and federal law independently applied the same standards to the same facts. State court findings on breach of fiduciary duty, failure to disclose, and misrepresentation were held under state law to preclude relitigation of those issues. Wright, p. 683.

The state proceeding below presented similar questions of fact. The state court decision did not rest on a determination of a matter within exclusive federal jurisdiction. For example, a state court determination on an anti-

trust defense in a contract suit is not binding in a federal antitrust suit. Id. In that case, application of federal law supported expert, uniform development of federal law in a trial governed by federal procedures. The case below does not present this situation, for the state court addressed no federal question.

Balancing the values served by exclusive federal jurisdiction against the values which justify the exercise of state court jurisdiction, the state values prevail. This balance favoring state preclusion rules is strengthened by this Court's decision in Marathon Pipe Line v. Northern Pipe Line, 458 U.S. 50 (1982). The plurality opinion in that case revoked the exercise by bankruptcy courts, acting as adjuncts of the district courts, of "the essential

attributes" of Article III judicial power. 458 U.S. at 87. Those "essential attributes" include reviewing the adequacy of other court's actions. Also note the federalism concerns raised in the concurring opinion. Those concerns strengthen the directive of the plurality. When state courts resolve questions which are not within exclusive federal jursidiction, federal courts are bound to follow state rules of preclusion. Under 28 U.S.C. §1738, the federal courts are bound by the state proceedings in the same manner as other courts of the same state. State law governs collateral estoppel effects of state judgments.

This Court should take this opportunity to clarify this often ignored question. It should provide guidance on the often litigated question of issue

preclusion, for at the core of that litigation is confusion over the roles of state and federal courts.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Fifth Circuit.

Respectfully submitted,

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By:
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April 5, 1984 COUNSEL FOR PETITIONER

CERTIFICATE OF SERVICE

I hereby certify that on this the 4th day of April, 1984, three copies of the Petition for Writ of Certiorari were mailed, first-class postage prepaid, to Eric R. Borsheim, Esquire, 910 West Avenue, Austin, Texas, 78701, Counsel for the Respondent. I further certify that all parties required to be served have been served.

Don L. Baker

DON L. BAKER

In the Matter of Ronald SHULER a/k/a Ronnie Shuler f/d/b/a Delta Motor Company, Bankrupt.

HAROLD V. SIMPSON AND COMPANY,
Plaintiff-Appellant,

v.

Ronald William SHULER,
Defendant-Appellee.

No. 83-1560
Summary Calendar.

United States Court of Appeals,
Fifth Circuit.

Jan. 20, 1984.

Before BROWN, TATE and HIGGINBOTHAM, Circuit Judges.

TATE, Circuit Judge:

In these proceedings arising under the Bankruptcy Code of 1978, 11 U.S.C. §§ 101 et seq., a creditor appeals from the rejection by the bankruptcy court, affirmed by the district court, of its contention that a debt was nondischargeable. We affirm, finding no merit to the creditor's principal contention that

the bankruptcy court was bound by collateral estoppel principles by a pre-bankruptcy state court determination that the debt was for services obtained by false pretenses--which, if so, excepted the debt from dischargeability under federal bankruptcy law.

The creditor company ("Simpson") filed a complaint in the bankruptcy proceedings to determine the dischargeability of a debt incurred by the bankrupt, Shuler. The creditor contended that the debt was excepted from dischargeability because it was a debt for obtaining services (the preparation of tax returns) by false pretenses. Section 523(a)(2)(A) of the Code, 11 U.S.C. § 523(a)(2)(A).[1] For proof of the debt's nondischargeability, the creditor

1. Section 523 ("Exceptions to discharge"), (a)(2)(A) provides:

Simpson relied solely upon the Texas state court proceedings that resulted in judgment in its favor against the bankrupt Shuler, wherein the state court, in granting a default judgment to Simpson, had recited that this creditor was entitled to judgment upon its cause of action based upon a "debt for obtaining by false pretenses the items furnished by Plaintiff [the creditor Simpson]."

The creditor Simpson contends that the bankruptcy court was bound by collateral estoppel to adopt the state court's finding that the debt was for services obtained by false pretenses and that, consequently, Simpson has borne

---

(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt--

* * * * * *

(2) for obtaining money, property, services, or an extension, renewal, or

its burden of proving the nondischargeability of the debt. We reject this contention, as inconsistent with the jurisprudential interpretations of the federal bankruptcy statute.

I.

In Brown v. Felsen, 442 U.S. 127, 99 S.Ct. 2205, 60 L.Ed.2d 767 (1979), the Supreme Court held that a bankruptcy court was not barred by res judicata from determining, independent of a state court judgment against a debtor, the nature of the debt in order to determine its dischargeability under the federal bankruptcy law. Finding that Congress intended to give the bankruptcy court exclusive jurisdiction to determine bankruptcy dischargeability issues, the

---

refinance of credit, by--
(A) false pretenses, a false

Court found that "the bankruptcy court is not confined to a review of the judgment and record in the prior state court proceeding when considering the dischargeability of respondent's debt." 442 U.S. at 138-39, 99 S.Ct. at 2213. While expressly leaving open the collateral estoppel question, the Court noted, however, that:

> This case concerns res judicata only, and not the narrower principle of collateral estoppel. Whereas res judicata forecloses all that which might have been litigated previously, collateral estoppel treats as final only those questions actually and necessarily decided in a prior suit.

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representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

* * * * * *

[Citations omitted.] If, in the course of adjudicating a state-law question, a state court should determine factual issues using standards identical to those of § 17 [of the former Bankruptcy Act; similar to § 523 of the present Bankruptcy Code] then collateral estoppel, in the absence of countervailing statutory policy, would bar relitigation of those issues in the bankruptcy court.

442 U.S. at 139 n. 10, 99 S.Ct. at 2213 n. 10.

In Carey Lumber Co. v. Bell, 615 F.2d 370 (5th Cir. 1980), this court affirmed the holding of the district court, which had affirmed the judgment of the bankruptcy court. We based our affirmance upon the district court's opinion, which we attached as an appendix. That opinion stated, although by way of dictum:

This court, of course, has no quarrel with the proposition, enunciated in these cases and urged by Bell, that a bankruptcy court faced with a claim of nondischargeability under § 17 and presented with a state court judgment evidencing a debt is not bound by the judgment and is not barred by res judicata or collateral estoppel from conducting its own inquiry into the character and, ultimately, the dischargeability of the debt. Like the Ninth Circuit in In re Houtman [568 F.2d 651 (1978)], this court would be constrained to reverse the bankruptcy court's decision if the bankruptcy judge had held himself to be bound by the state court judgment. That, however, is not the case.

615 F.2d at 377. The court went on to affirm a summary judgment that held that the debt was nondischargeable, based upon a state court consent judgment that contrained a detailed recitation of facts that showed a federally nondischargeable basis for the debt. The judgment was introduced without opposing showing, and the court therefore concluded:

> The bankruptcy court was correct in determining that no issue of fact existed as to the recitations in the state court judgments. It therefore properly accepted these recitations as true, and correctly found that they required the legal conclusion that the debt owed Carey by Bell was nondischargeable in bankruptcy under § 17(a)(4).

615 F.2d at 378.

We thus in Carey Lumber Co. v. Bell upheld rationale that neither res judicata nor collateral estoppel bar a bankruptcy court from receiving evidence as to facts by which that court may determine the character and, ultimately, the dischargeability of the debt. We there also, however, affirmed the holding that, nevertheless, the recitations of the state court judgment may be considered as evidence that, if uncontroverted, may be sufficient upon which to base a holding that the debt is nondischargeable as measured by the federal standard of dischargeability.

We did not in Carey Lumber Co. v. Bell reach or consider the issue as to whether "collateral estoppel, in the absence of countervailing statutory policy would bar relitigation of . . . factual issues . . . actually and necessarily

decided in [the] prior suit." Brown v. Felsen, supra, 442 U.S. at 139 n. 10, 99 S.Ct. at 2313 n. 10 (emphasis added). However, in the sparse subsequent decisions on the issue, the district and bankruptcy courts of the present and former Fifth Circuit, as in the present instance, have held that collateral estoppel--arising from an earlier nonbankruptcy suit's determination of subsidiary facts that were actually litigated and necessary to the decision--may properly be invoked by the bankruptcy court to bar relitigation of those issues, even though the bankruptcy court retains the exclusive jurisdiction to determine the ultimate question of the dischargeability under federal bankruptcy law of the debt, upon the facts so based and other evidence before the court.

An excellent statement of the reasons for these rulings is contained in Franks v. Thomason, 4 B.R. 814, 820-21 (Bkrtcy.N.D. Ga. 1980):

> The bankruptcy court may not relitigate the entire case; to do so would do violence to judicial finality, a fundamental tenet of our judicial system. Congress only intended for that policy to give way to the extent necessary to enable the bankruptcy court to make the ultimate determination of dischargeability of debts under section 17a(8). Those facts that were actually litigated and necessary to the decision in the court that rendered the judgment, and that are discernible from the record of the case, should not be reopened absent a compelling reason to avoid injustice. . . . The bankruptcy judge

must necessarily tailor his application of collateral estoppel to the circumstances of the case before him, consistent with its purposes and the countervailing intent of Congress. The ultimate finding of whether [a debt is nondischargeable, as "defined" by the bankruptcy law] is solely the province of the bankruptcy court; those subordinate factual findings that are necessary to that ultimate determination, that have not been actually and necessarily litigated or that are not discernible from the record, must also be determined by it after hearing all relevant evidence that is presented by the parties.[2]

2. The applicability of collateral estoppel thus stated is in accord with the general test for collateral estoppel in this circuit.

Accord, In re Whitmore, 7 B.R. 835, 838 (Bkrtcy. N.D. Ga. 1980), cf., In re Waters, 20 B.R. 277, 280 (Bkrtcy. W.D. Tex. 1982).

[1] This rationale and the resulting conclusion--that collateral estoppel may apply to subsidiary facts actually litigated and necessarily decided--represents the predominant view of the other circuits that have considered the issue.[3] In the present bankruptcy proceedings, the bankruptcy court applied these principles in determining the dis-

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This Court has stated that the three traditional requirements for the application of the doctrine of collateral estoppel are: (i) the issue to be precluded must be identical to that involved in the prior action, (ii) in the prior action the issue must have been actually litigated, and (iii) the determination made of the issue in the prior action must have been necessary to the resulting judgment.

White v. World Finance of Meridian, Inc., 653 F.2d 147, 151 (5th Cir. 1981).

3. The several circuits have developed somewhat different rules as to this issue. Com-

chargeability of the debt represented by the state court judgment. We find no error of law in its so doing.

II.

In its appeal, the creditor Simpson contends that the only evidence before the bankruptcy court was to the effect that the debt for services was obtained through false pretensions, and that therefore the bankruptcy court was clearly erroneous in not sustaining its complaint that the debt was nondischargeable under Section 523(a)(2)(A). However, the only evidence the creditor presented in the bankruptcy action was

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pare Spilman v. Harley, 656 F.2d 224, 227-28 (6th Cir. 1981) and Matter of Ross, 602 F.2d 604, 607 (3rd Cir. 1979) (holding that a prior state court judgment can have collateral estoppel effect in a bankruptcy proceeding) with In Re Rahm, 641 F.2d 755, 757 (9th Cir. 1981), cert. denied, 454 U.S. 860, 102 S.Ct. 313, 70 L.Ed.2d 157 (1981)

with regard to the state judicial proceedings leading to judgment, and answers to interrogatories and admissions with regard thereto. The latter confirmed that the only evidence produced in the state court proceedings to support the default judgment was the com-

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(holding that a prior state court judgment has no collateral estoppel effect in a bankruptcy court, but may establish a prima facie case of nondischargeability). See also In Re Houtman, 568 F.2d 651, 655 (9th Cir. 1978) (holding prior to the Supreme Court's decision in Brown v. Felsen, supra, that a state court judgment based on fraud establishes only a prima facie case that a debt is nondischargeable in a bankruptcy action).

Spilman v. Harley, supra, contains an excellent discussion of the jurisprudential holdings as to this issue, and of the reasons why, in proper circumstances, collateral estoppel should apply. 656 F.2d at 226-28. It concludes, 656 F.2d at 228:

> Thus, before applying the doctrine of collateral estoppel, the bankruptcy court must determine if the issue was actually litigated and was necessary to the decision in the state court. To do this, the bankruptcy court should look at the entire record of the state proceeding, not just the judgment, [citations omitted] or

plaint[4] and the affidavit verifying the invoices for income tax preparation sued upon.[5]

Thus, the actual issue presented is whether the bankruptcy judge erred in finding that the creditor Simpson failed

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hold a hearing if necessary [citations omitted].

4. Simpson's state court petition reads in pertinent part as follows:

* * * * * *

2. Facts. As shown in the attached statement of account, Plaintiff sold to Defendant goods, services, wares, and merchandise, which Defendant accepted and thereby became bound to pay to Plaintiff the stated price thereof, which is a reasonable and fair, usual and customary price.

3. Debt. The balance due and owing to Plaintiff on said account is $568.75. Although often requested, Defendant has failed and refused to pay the amount due. This debt is for obtaining the items specified by false pretenses, both inclusive and exclusive of representations of financial condition.

* * * * * *

5. The affidavit in support of the invoices reads as follows:

to carry its burden of proof that the debt was nondischargeable, which--since the state court record is the only evidence relied upon by the creditor--in essence presents the issue of whether the bankruptcy court erred in failing through collateral estoppel principles to accept the alleged determination by

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"BEFORE ME, the undersigned authority, on this day personally appeared HAROLD V. SIMPSON [affiant] who is the Senior partner [official capacity] for the Harold V. Simpson & Company, CPA's [creditor] and upon oath stated that the claim evidenced by the attached documents is within the knowledge of affiant, just and true, that it is due and that all just and lawful offsets, payments and credits have been allowed, that such documents were made in the regular course of business, that it was the regular course of business for an employee or representative of the business with personal knowledge of such act, event or condition to make such memorandum or record or to transmit information thereof to be included in such memorandum or record, and that it was made at or near the time of the act, event or condition or reasonably soon thereafter."

the state court in its default judgment[6] that the debt was for services obtained by false pretenses.

[2] The bankruptcy court did not err in failing to accord collateral estoppel effect, for bankruptcy dischargeability purposes, to the alleged false-pretense determination in the state court judgment.

Unlike the consent judgment in Carey Lumber Co. v. Bell, supra, see 615 F.2d at 378, the judgment in the present case did not contain detailed facts suffi-

6. Having determined as a threshold matter that the state proceedings here cannot factually be accorded collateral estoppel effect, the bankruptcy court did not reach, nor do we, the further issue of whether a default judgment meets the "actually litigated" test for collateral estoppel for bankruptcy dischargeability determinations. According to Spilman v. Harley, supra, the preponderant view (citing decisions) is that a default judgment does not through collateral estoppel bar relitigation in the

cient as findings to meet the federal test of nondischargeability; it contained merely a conclusory statement that the plaintiff was entitled to judgment on a false-pretense cause of action.[7] Nor, on examining the pleadings (see note 4, supra) and the attached affidavit (see note 5, supra)--with the judgment, the entire record of the state proceedings--, are any facts discernible that show the specific false-pretense

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bankruptcy court. 656 F.2d at 228; see, to same effect, Franks v. Thomason, supra, 4 B.R. at 821.

7. The state court judgment in its entirety reads as follows:

JUDGMENT

On this day came on to be heard the above styled and numbered cause. The Court finding that Defendant, though duly cited to appear and answer herein, has wholly failed to appear and answer herein, that appearance day for the Defendant has passed, that Plaintiff's cause of action is based upon a liquidated demand and debt for obtaining by false pretenses the items furnished by Plaintiff, and that Plaintiff is entitled to judgment as prayed for:

conduct, by which the federal bankruptcy court might determine the creditor's claim of nondischargeability, measured by federal bankruptcy standards.[8] If only for these reasons,[9] the bankruptcy

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It is, accordingly, ORDERED, ADJUDGED and DECREED that Plaintiff, Harold V. Simpson & Company, have and recover of and from Defendant, Ronald W. Shuler, doing business as Bill Shuler Marketing Co., judgment in the sum of $808.52, together with interest thereon from date of judgment at the rate of nine percent (9%) per annum until paid, and for all costs of court in this behalf expended, for all of which let execution issue. In event of any appeal from or attack upon the effect of this judgment in any court, state or federal, direct or indirect, including bankruptcy proceedings, further and additional reasonable attorney's fees of $2,500.00 for each such proceeding in each such court are hereby awarded to the extent this court has jurisdictional power to so order.

8. In fact, the only evidence in support of the default judgment was the invoices noting Shuler's debt and an affidavit verifying the genuineness of the debt (see note 5), neither of which includes any indication of the "false pretenses" through which the creditor Simpson's tax services were allegedly obtained.

9. We further note that other prerequisites for collateral estoppel were not met. Under

court--unable to discern from the record the subsidiary facts upon which the false-pretense allegation was made--properly refused to accord collateral estoppel effect to the conclusory false-pretense "determination" in the state court judgment.

[3] We thus find no merit to Simpson's contentions on its appeal.[10]

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the showing of the entire state proceedings, in this case the false-pretense issues were not shown to have been factually presented to the court so as to have been "actually litigated." Nor, on this judgment for the actual amount of a liquidated account, did the judgment "necessarily determine" any false-pretense issue; the debtor owed the amount due for the creditor's services in preparing his income tax returns, with or without false pretenses.

10. Simpson also contends that the bankruptcy court failed to give "full faith and credit" to the judgment of the state court as required by 28 U.S.C. § 1738, which provides in part that state judicial proceedings "shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the Courts of such State."

Conclusion

Finding no merit to the creditor Simpson's contentions, we AFFIRM the judgment of the district court affirming the bankruptcy court's determination of dischargeability.

AFFIRMED.

The full faith and credit due a state court judgment is of course manifested by the res judicata or collateral estoppel effect accorded to that judgment. See Allen v. McCurry, 449 U.S. 90, 96, 101 S.Ct. 411, 415-16, 66 L.Ed.2d 308 (1980). Where, as in bankruptcy, the res judicata or collateral estoppel effect of state court judgments has been limited by competing federal interests, see Brown v. Felsen, supra, 442 U.S. at 136-37, 99 S.Ct. at 2211-12, the full faith and credit owing to the state court judgment may be correspondingly limited. Since the courts below properly assessed the collateral estoppel effect of the state court judgment in the present federal bankruptcy case, the full faith and credit principles of § 1738 have not been violated.

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF TEXAS
AUSTIN DIVISION

HAROLD V. SIMPSON & COMPANY	§	
	§	
vs.	§	A-82-CA-672
	§	
RONALD WILLIAM SHULER	§	

ORDER AFFIRMING BANKRUPTCY COURT'S DECISION

On this date the Court considered the above-styled and numbered cause. The Court hereby affirms the Bankruptcy Court's decision for the reasons set forth in its opinion.

IT IS SO ORDERED.

Signed this 14 day of July, 1983.

_____
Fred Shannon,
United States District Judge

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TEXAS
AUSTIN DIVISION

IN RE:

RONALD WILLIAM SHULER,
aka RONNIE SHULER,
fdba DELTA MOTOR COMPANY,
fdba SHULER MOTOR COMPANY,

BANKRUPTCY NO. 1-81-00344-E

DEBTOR

HAROLD V. SIMPSON & COMPANY,

PLAINTIFF

VS.

ADVERSARY NO. 1-81-0166-E

RONALD WILLIAM SHULER,

DEFENDANT

JUDGMENT

On the 11th day of March, 1982, came on to be heard the Complaint of Harold V. Simpson & Company, Plaintiff, to determine dischargeability of a debt incurred by Ronald William Shuler, aka Ronnie Shuler, fdba Delta Motor Co., fdba Shuler Motor Co., Defendant. The

parties appeared in person and by attorneys and announced ready for trial.

The Court finds as follows:

(a) That the debt made the purpose of this adversary proceeding was incurred for the preparation of Debtor's 1977, 1978, and 1979 Individual Income Tax Returns.

(b) That the Plaintiff's judgment in the state court case of Harold V. Simpson & Co., vs. Ronald Shuler, Cause No. 100,978, in the County Court at Law No. 1, Travis County, Texas, was taken by default when the Defendant failed to appear and answer therein.

(c) The only evidence offered to support the state court default judgment was the account documents attached to Plaintiff's Original Petition in that case.

(d) That the Plaintiff relied solely upon its Original Petition and the attachments thereto in the state court case to sustain and support its motion for default judgment.

(e) That this court held, in a case involving the same issue (Adversary No. 1-81-0031), that full faith and credit and res judicata theories do not confine a bankruptcy court to a review of the judgment and record in a prior state court proceeding when determining dischargeability of a debt.

(f) That estoppel does bar a bankruptcy court from relitigating those issues previously litigated in state court proceedings if:

1. The issues are identical to those adjudicated in state court;

2. The issues were actually litigated in a prior state court proceeding involving

the same parties as those before the bankruptcy court; and

3. The issues were necessary to the prior judgment.

(g) That, since the above conditions were not met in the state court proceeding, and the Court is presented with a limited record, it is unable to determine the precise factual issues litigated or the standards applied by the state court to reach its conclusions of law, and must look behind the state court default judgment and its bare recitals.

(h) That the other evidence presented to the Court by the Plaintiff is insufficient to establish the non-dischargeability of the debt.

Accordingly, this Court finds it is not bound by collateral estoppel to adopt the state court's findings. The

Plaintiff has failed to sustain its burden of proof and the debt is hereby found dischargeable.

IT IS, THEREFORE, ORDERED, ADJUDGED, AND DECREED, that the debt sought to be declared non-dischargeable should be, and it is hereby, DISCHARGED in bankrupty.

Accordingly, Plaintiff's request for attorney's fees and exemplary damage is hereby DENIED.

SIGNED AND ENTERED this 18 day of November, 1982.

_____
JOSEPH C. ELLIOTT
UNITED STATES BANKRUPTCY
JUDGE

NO. 100,978

HAROLD V. SIMPSON & COMPANY	X X X	COUNTY COURT AT LAW NO. 1
VS.	X X	OF
RONALD W. SHULER	X X	TRAVIS COUNTY, TEXAS

JUDGMENT

On this day came on to be heard the above styled and numbered cause. The Court finding that Defendant, though duly cited to appear and answer herein, has wholly failed to appear and answer herein, that appearance day for the Defendant has passed, that Plaintiff's cause of action is based upon a liquidated demand and debt for obtaining by false pretense the items furnished by Plaintiff, and that Plaintiff is entitled to judgment as prayed for:

It is, accordingly, ORDERED, ADJUDGED and DECREED that Plaintiff, Harold V.

Simpson & Company, have and recover of and from Defendant, Ronald W. Shuler, doing business as Bill Shuler Marketing Co., judgment in the sum of $808.52, together with interest thereon from date of judgment at the rate of nine percent (9%) per annum until paid, and for all costs of court in this behalf expended, for all of which let execution issue. In event of any appeal from or attack upon the effect of this judgment in any court, state or federal, direct or indirect, including bankruptcy proceedings, further and additional reasonable attorney's fees of $2,500.00 for each such proceeding in each such court are hereby awarded to the extent this court has jurisdictional power to so order.

SIGNED 7-2-81.

JUDGE PRESIDING

Office - Supreme Court, U.S.
FILED
JUN 16 1984
ALEXANDER L. STEVAS,
CLERK

NO. 83-1634

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1983

HAROLD V. SIMPSON & COMPANY, Petitioner

VS.

RONALD WILLIAM SHULER, Respondent

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

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13 pp

BEST AVAILABLE COPY

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STATEMENT OF THE CASE

Harold V. Simpson & Co. filed suit in a Texas County Court at Law against Ronald W. Shuler based on a sworn account for services rendered to Shuler incident to the preparation of his tax returns. In addition to the usual pleadings to support recovery on the debt (sworn account), the plaintiff's attorney deftly included some additional pleadings tracking the language of 11 USC 523 (a)(2)(A). The pleadings were conclusory and pled no facts upon which the plaintiff Simpson relied to show false pretenses, false representations, or actual fraud. Simpson's case being adequately pled on the sworn account, the additional fraud pleadings were not necessary to Simpson's recovery.

Shuler did not answer Simpson's suit, or otherwise appear and defend in any manner. Simpson obtained a judgment by default which recited that Simpson's cause of action was based on a liquidated debt for obtaining by

false pretenses the services furnished. The recitation in the default judgment concerning the false pretenses found its basis only in Simpson's pleadings, and the state trial court received virtually no other evidence on that issue.

Some months later, Shuler filed a petition for relief under Chapter 7 of the Bankruptcy Code. Simpson filed a complaint in the bankruptcy proceeding objecting to the discharge of its debt on the basis that it was one "for obtaining money, property, or services by false pretenses other than a statement respecting financial condition." Upon trial of the complaint before the bankruptcy judge, Simpson relied solely on the "false pretense" recitations of its state court judgment; it offered no evidence to support the false pretense allegations in its complaint, and it offered no evidence that any evidence of that nature was considered by the state court judge. Indeed it did not

because it could not. There was simply no fraud in the case which could be proved in any forum. But if it could raise its illegitimate and completely unfounded pleading to a judgment entitled to the the sanctuary of res judicata, then it would have created the collection lawyer's dream--a whole generation of default judgments which were not dischargeable in bankruptcy, obtained with the ease of the entry on one simple sentence in their word processors. With the financial implications of such a possibility being obvious, so began the trek of Ron Shuler's $800 debt to this court.

SUMMARY OF ARGUMENT

The U.S. Bankruptcy Court has exclusive jurisdiction to determine the dischargeability of a debt in a bankruptcy proceeding. No state court has jurisdiction to determine the issue of dischargeability,

and hence 28 USC 1738 does not extend full faith and credit to any state court judgment to the extent such judgment purports to decide the issue of dischargeability. Being exclusively a creature of federal law, federal preclusion and collateral estopple rules govern the effect of a state court judgment when it is sought to be utilized by any party before the bankruptcy court on the issue of dischargeability.

REASONS FOR DENYING THE WRIT

1. THE DECISION BELOW DOES NOT CONFLICT WITH THE DECISIONS OF THE SUPREME COURT AS TO THE PROPER APPLICATION OF 28 U.S.C. 1738.

The Petitioner cites Allen v. McCurry, 449 U.S. 90, 96 (1980) for the proposition that the federal courts should apply state law in determining the collateral estopple effect of prior state court adjudication. In the Allen case, the state criminal trial court refused, under Fourth and Fourteenth

Amendment challenges, to supress certain evidence seized in a narcotics raid. In a subsequent civil suit against the arresting officers under 42 USCS 1983, this court sustained the District Court's use of collateral estopple to prevent the defendant from relitigating the search-and-seizure question adversly decided against him in the state court.

The difference in the Allen case and the instant case is readily apparent. No citations are necessary for the proposition that both the state and federal courts have jurisdiction to decide Fourth Amendment issues. In this case, however, only the federal courts, have jurisdiction to decide the issue of dischargeability of a debt in bankruptcy. The bankruptcy court has exclusive jurisdiction to decide dischageability questions, and no state court judgment may may stand as a res judicata bar on that issue. Brown v. Felsen, 442 U.S. 127

(1979). Since the dischargeability issue cannot be adjudicated in state court, it is patently ridiculous to apply state law in determining the collateral estopple effect of that which cannot be adjudicated in the state forum. It is not surprising then that the Fifth Circuit applied the federal collateral estopple test to that issue which was exclusively a federal issue.

2. THE DECISION BELOW DOES NOT RAISE SIGNIFICANT AND RECURRING PROBLEMS OF COLLATERAL ESTOPPLE UNDER 28 U.S.C. 1738 IN BANKRUPTCY DISCHARGEABILITY QUESTIONS.

The only recurring and significant problem which the Fifth Circuit's decision raises is that it prevents collection lawyers from taking one the easy way. It forces them to actually prove up their dischargeability case in the bankruptcy court.

The Fifth Circuit's application of collateral estopple fully insures that issues honestly litigated and determined in prior

state court proceedings may be considered by the bankruptcy court in determining dischargeability issues. In appropriate instances the state court judgment may be conclusive. Carey Lumber Co. v. Bell, 615 F.2d 370 (5th. Cir. 1980) The application of federal preclusion and collateral estopple rules requires that the dischargeability issue be fairly addressed, and the application of these rules is consistent with the concept of exclusive federal jurisdiction.

Recognizing this, the Petitioner urges this Court to abandon the exclusive jurisdiction approach it adopted in Brown v. Felsen, supra. We are told that the reasons for exclusive federal jurisdiction are not present today. We are further assured that there is "no danger of abuse in a pre-bankruptcy suit," when it is obvious what kind of abuse Petitioner seeks to achieve with its pre-bankruptcy suit. Absent the

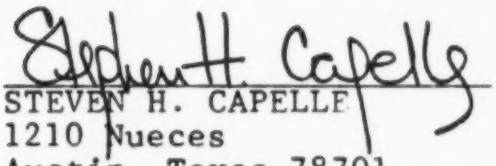
exclusive jurisdiction restraint, unwitting state court judges could determine the dischargeability issue by entering default judgments which parrot completely unfounded fraud pleadings in a petition.

The Fifth Circuit's decision governing the role of a state court default judgment in the determination of the dischargeability of a debt in a bankruptcy proceeding adequately and fairly protects the debtor from the unfounded fraud claim, and insures that the defrauded creditor have his day in court. The parity which presently exists is derived from the exclusive federal jurisdiction in dischargeability questions, and any departure from the exclusive jurisdiction rule would only serve the unscrupulous.

CONCLUSION

For these reasons, a writ of certiorari should not issue to review the judgment of the Fifth Circuit.

RESPECTFULLY SUBMITTED,



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ATTORNEY FOR RESPONDENT

CERTIFICATE OF SERVICE

I hereby certify that on this the 14TH day of June, 1984, three copies of this Brief in Opposition was mailed via First Class U.S. Mail to Don L. Baker, Esq., Baker and Price, 314 West 11th. St., Suite 500, Austin, Texas 78701, Attorney for the Petitioner, and further certify that all parties required to be served have been served.

Stephen H. Capelle

STEPHEN H. CAPELLE